



Operating Deficit Guide for Municipal Utilities

March 2021

Presented by Manitoba Public Utilities Board Staff



Topics Covered by this Presentation:

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The Public Utilities Board Oversight

- ▶ The Board Authority - *The Public Utilities Board Act* - Section of 74(1) - **General supervision over utilities**
- ▶ The Manitoba municipalities, excluding the City of Winnipeg, are responsible for managing the utilities.
- ▶ The Board's primary focus for Water & Wastewater Utilities is:
 - the reasonableness of rates including surcharges;
 - approving operating deficits, and appropriate recovery of deficits; and
 - ensuring the financial sustainability of the utility.



The Public Utilities Board Oversight

The Municipal Act set out provincial requirements pertaining to the operation of water and wastewater utilities' deficits.

Section 164(4) - Budgeted Deficits

Utilities expenditures not to exceed transfers and revenue

The council must ensure that the amount of estimated revenue and transfers provided for in the utility budget is not less than the amount of estimated expenditures in respect of the utility unless, before adopting the operating budget, the council obtains The Public Utilities Board's written approval, which may include any condition the Board considers necessary or advisable.

Section 165(2) - Actual Deficits

Council to obtain approval for anticipated deficiency in utility

When a council determines during a fiscal year that expenditures of a utility are likely to exceed the revenue and transfers provided for in the utility budget, the council must immediately advise The Public Utilities Board in writing and may incur a deficiency with the Board's written approval, which may include any condition the Board considers necessary or advisable.



The Public Utilities Board Oversight

- ▶ **Board Order No. 151/08** - Water and/or Sewer Utilities Financial Reporting Requirements
- ▶ These requirements pertain to budgeted, anticipated and year-end operating deficits, as well as transfers to operations.
- ▶ Required to establish a plan to address deficits.
 - Accumulated surplus;
 - Utility Reserves;
 - Rate Riders or Flat Rate; or
 - Other, such as levies approved by the Board.
- ▶ Utility's Accumulated Surplus account not to be reduced below 20% of prior year's operating expenditures.



Public Sector Accounting Board Standards (PSAB)

- ▶ As of January 1, 2009, the Public Sector Accounting Board (PSAB) set new standards for all public sector accounting to transition to accrual accounting.
- ▶ The Government of Manitoba adopted the national standards.
- ▶ The Public Utilities Board issued **Board Order No. 93/09** on June 9, 2009, providing assistance and direction for Municipal utilities.
- ▶ PSAB standards have had a significant impact on annual financial reporting and utility rate setting.
 - PSAB standards involve **non-cash** entries.
- ▶ Reference Manuals for The Tangible Capital Asset (TCA) and Financial Statements were released in June 2007. These manuals were developed in partnership between the AMM and MB Intergovernmental Affairs and are available from Municipal Relations.
- ▶ All Municipalities are required to be PSAB compliant now.



Deficit Overview & Definitions

1. What is a Utility Operating Deficit?
2. Deficit Definitions: Budgeted, Anticipated & Actual



What is a Utility Operating Deficit?

- ▶ Unforeseen expenditures may arise and utilities could incur an operating deficit.
- ▶ Municipally owned public utilities are expected to operate on a breakeven basis.
- ▶ **Municipalities must apply to the Public Utilities Board for approval of any operating deficit and recovery methodology, if it exceeds \$10,000 or 5% of the utility's operating budget.**
- ▶ Typically, deficit recovery is through the use of accumulated surplus funds, the utility reserve funds, rate rider, or flat rate, or a combination of these methods.
- ▶ There are three types of deficit Applications:
 - ▶ Budgeted Deficit
 - ▶ Anticipated Deficit
 - ▶ Actual/Audited Deficit



Deficit Definitions - Budgeted Deficit

- ▶ **Budgeted Operating Deficit:**
 - ▶ Deficit is budgeted in the Utility's annual budget.
 - ▶ Usually due to a scheduled minor upgrade or repair where surplus/reserve funds do not fully cover.
 - ▶ Application to be filed on or before April 1 of the budget year.
 - ▶ This is rare, and must be PSAB compliant
 - ▶ Actual deficits based on audited financials give a better financial picture.
 - ▶ Rate Rider Calculation must be considered.



Deficit Definitions - Anticipated Deficit

▶ Anticipated Operating Deficit:

- ▶ Deficit is suspected because an unforeseen expenditure has arisen or revenues have been reduced.
- ▶ Usually based on known circumstances and/or unaudited financials.
- ▶ Application filed within 60 days the expenditure is incurred.
- ▶ This is rare.
- ▶ Actual deficits based on audited financials give a more accurate financial picture.
- ▶ Rate Rider Calculation must be considered.



Deficit Definitions - Actual/Audited Deficit

▶ Actual Operating Deficit:

- ▶ Deficit is confirmed by the Municipal auditor in the completed and approved Audited Financial Statements.
- ▶ Deficit is before any transfer on Schedule 9 in the Audited Financial Statements
- ▶ All deficits must be recovered, as per the Board's Guidelines.
- ▶ Applications must be filed as soon as a deficit is known.
- ▶ Rate Riders (for metered utilities) or flat rate charges (for unmetered utilities) to be calculated using final numbers.



Working Capital Calculation



Working Capital Calculation

- ▶ Established in **Board Order No. 93/09**
- ▶ Maintain a minimum working capital surplus of 20% of annual expenses.
- ▶ The working capital surplus is the Utility fund balance, excluding any capital related items, plus Utility long term debt and reserves.
- ▶ The Working Capital calculation is one indicator used by the Board to review the financial health of the Utility and how liquid it is.
- ▶ Where the Working Capital Target is less than the 20% target, a minimum provision of 1% of expenses may be built into the revenue requirements until such a time as the target is reached.

Working Capital Calculation - Surplus

	2018
Utility Fund Accumulated Surplus	\$449,365
Deduct Tangible Capital Assets (TCA)	(\$235,811)
Add Long Term Debt	\$0
Add Utility Reserves	\$0
Equals Working Capital Surplus (Deficit)	\$213,554
Expenses	\$109,111
20% of Expenses (Target)	\$21,822

Schedule 8

Schedule 6

Schedule 9

Working Capital Calculation - Deficit

	2018
Utility Fund Accumulated Surplus	\$2,366,490
Deduct Tangible Capital Assets	(\$3,802,818)
Add Long Term Debt	\$896,695
Add Utility Reserves	\$20,082
Equals Working Capital Surplus/(Deficit)	(\$519,551)
Expenses	\$575,331
20% of Expenses (Target)	\$115,066



How to Check & Prepare for a Deficit

1. Where to find the Deficit in the Financial Statements
2. Review Public Utilities Board Note in Financial Statements



Where to Find The “Audited” Deficit

- ▶ The Schedule of Utility Operations is found in the Municipal Financial Statements, titled **Schedule 9 - Schedule of Utility Operations**, but in some cases can be found as **Schedule 8** where an old template of the Financial Statements is being used.
- ▶ The audited Surplus or Deficit for the Utility is found as a line in the Financial Statements after the Total Expenses line, but before Utility Transfers.
- ▶ It may be called any of the following:
 - ▶ Net Revenues
 - ▶ Net Operating Surplus
 - ▶ Excess of Expenses Over Revenue
 - ▶ Net Operating Surplus (Deficit)
 - ▶ Net Deficit

Schedule 9 - Examples

Total expenses	<u>1,014,711</u>	<u>954,033</u>	<u>885,240</u>
NET REVENUES	(8,939)	(18,709)	(55,675)
TRANSFERS			
Transfers from (to) operating fund	-	66,189	-
Transfers from (to) reserve funds	<u>32,000</u>	<u>40,616</u>	<u>59,960</u>
CHANGE IN UTILITY FUND BALANCE	<u><u>\$ 23,061</u></u>	88,096	4,285
FUND SURPLUS, BEGINNING OF YEAR		<u>2,693,053</u>	<u>2,688,768</u>
FUND SURPLUS, END OF YEAR		<u><u>\$ 2,781,149</u></u>	<u><u>\$ 2,693,053</u></u>

Schedule 9 - Examples

Total expenses	<u>223,215</u>	<u>276,959</u>	<u>273,352</u>
NET OPERATING SURPLUS	56,216	(12,560)	763
TRANSFERS			
Transfers from (to) operating fund	(17,442)	12,015	-
Transfers from (to) capital	(28,630)	-	-
Transfers from (to) reserve funds	<u>(10,144)</u>	<u>(10,144)</u>	<u>59,664</u>
CHANGE IN UTILITY FUND BALANCE	<u>\$ -</u>	(10,689)	60,427
FUND SURPLUS, BEGINNING OF YEAR		<u>1,180,109</u>	<u>1,119,682</u>
FUND SURPLUS, END OF YEAR		<u>\$ 1,169,420</u>	<u>\$ 1,180,109</u>



Public Utilities Board Note in Audited Financial Statements

- ▶ Municipalities should work closely with their auditor(s) to ensure the Public Utilities Board Note in the Consolidated Financial Statements is complete and accurate.
- ▶ If omitted, incomplete, or incorrect, it limits the Board's ability to assess a utility's financial position, and the Municipality's ability to set appropriate rates to sustain the utility and its operations.
- ▶ This note should include any capital grants, contributed assets and the in-year amortization associated with each.
- ▶ This information can eliminate the need to apply for a deficit or significantly reduce a deficit.



Public Utilities Board Note in Audited Financial Statements

19. Public Utilities Board

The Public Utilities Board (PUB) regulates the rates charged by all water and sewer utilities, except the City of Winnipeg utility and those utilities operated by the Manitoba Water Services Board. PUB has the authority to order any owner of a utility to adopt uniform and prescribed accounting policies. PUB's prescribed accounting policies on tangible capital assets and government transfers do not meet the recommendations of PSAB.

No capital grants have been deferred and amortized in these financial statements.

Public Utilities Board Note in Audited Financial Statements

19. Public Utilities Board

The Public Utilities Board (PUB) regulates the rates charged by all water and sewer utilities, except the City of Winnipeg utility and those utilities operated by the Manitoba Water Services Board. PUB has the authority to order any owner of a utility to adopt uniform and prescribed accounting policies. PUB's prescribed accounting policies on tangible capital assets and government transfers do not meet the recommendations of PSAB.

For information purposes, the Municipality has deferred the capital grants it has received in the past for its utilities and amortized them over the useful life of the related tangible capital asset.

No capital grants have been deferred and amortized in these financial statements.

Water services:

Description of Utility	Unamortized Opening Balance	Additions During Year	Amortization During Year	Unamortized Balance Ending
Cartier Utility	\$ 8,309,571	\$ -	\$ 322,426	\$ 7,987,145
Oakville Utility	481,853	-	22,180	459,673
	<u>\$ 8,791,424</u>	<u>\$ -</u>	<u>\$ 344,606</u>	<u>\$ 8,446,818</u>



How to Calculate the Deficit

1. PUB Schedule 9 Form
2. Regulatory Adjustments
3. Example Calculations

PUB Schedule 9

- ▶ This template has been provided by the Board for utilities to calculate Utility Deficits and account for regulatory calculations.
- ▶ Available on the Board’s website.
- ▶ The PUB Schedule 9 must match the audited financial Utility Schedule 9, with the exception of the regulatory calculations seen in the blue rows at the bottom.

Net Revenue before adjustment	-	-	-
Deduct Deficit recovered in Current Year	-	-	-
Deduct Contributed TCAs Current Year (Note 19)	-	-	-
Deduct Capital Grants Current year (Note 19)	-	-	-
Add Amortization of Capital Grants (Note 19)	-	-	-
Add Amortization of Contributed TCAs (Note 19)	-	-	-
NET OPERATING SURPLUS	-	-	-



Regulatory Adjustments

- ▶ The form shows the applicant how to calculate a deficit by removing the amounts that are not true revenue or one time revenue to be deducted from the Utility's Net Revenue such as:
 - ▶ Deficit recovery revenues from previous deficits,
 - ▶ Debenture surcharge revenue
 - ▶ Contributed TCAs, and
 - ▶ Capital Grants.
- ▶ The form also shows what approved regulatory additions can be made during year based on the PUB Note:
 - ▶ Annual amortization of capital grants, and
 - ▶ Annual amortization of contributed assets.
- ▶ These adjustments either decrease the actual deficit amount or in some cases eliminate the deficit.



Regulatory Adjustments: Deductions

Deficit Recovered in Current Year

- ▶ Applies to a previously approved deficit recovery through a rate rider, the utility needs to calculate the total rate rider revenue recovered in the current year and subtract it from the operating results for the year.
- ▶ The total recovered is the minimum the utility must have in that year's annual operating surplus to break even.
- ▶ For example, if a utility had a 2015 deficit to be recovered by rate rider of \$12.00 per customer quarterly, with 200 utility customers, that would indicate rate rider revenue of $12 \times 4 \times 200 = \$9,600$ per year.
- ▶ While recovering a prior deficit, the utility still needs to recover its operating costs through its rates, so the utility must have a surplus of at least \$9,600 to break even.
- ▶ To continue our example, assume the surplus for 2017 is less than \$9,600; then the 2015 deficit recovery is going towards the current year's operations, rather than recovering for 2015. The utility would have another operating deficit for 2017, which would be a strong indicator that the current utility rates are inadequate.



Regulatory Adjustments: Deductions

Contributed Tangible Capital Assets (TCAs) in Current Year:

- ▶ Contributed TCAs are those assets which were gifted to a utility at no cost.
- ▶ A developer may be responsible for the cost of installing the utility infrastructure, with the agreement/understanding it will be donated to the municipality at some determined point in the future.
- ▶ If the utility has not received any contributed TCAs in the current year, there is no information to enter on this line.
- ▶ *NOTE: This does not refer to assets that the utility has acquired by any means other than donation.*



Regulatory Adjustments: Deductions

Capital Grants in Current Year:

- ▶ Capital grants are funds allocated to the municipality for capital purchases, typically from the Federal or Provincial Government.
- ▶ The value of the capital grants received in the current year will also be found on Schedule 9 - Schedule of Utility Operations of the audited financial statements, under the Revenue section.
- ▶ If the utility has not received any capital grant funding in the current year, there is no information to enter on this line.
- ▶ *NOTE: This does not refer to any funding that is for operating expenses.*



Regulatory Adjustments: Additions

Amortization of Capital Grants:

- ▶ Available in the Public Utilities Board Note (PUB Note) in the audited financial statements.
- ▶ If it is not, the municipality should contact their auditor to receive this information .
- ▶ **Applicable to Utility** assets with a current net book value that were funded in any way by capital grants should have amortization of capital grants to offset the utility deficit.
- ▶ The Manitoba Water Services Board (MWSB) may also have information regarding the history of capital grants received by the utility.



Regulatory Adjustments: Additions

Amortization of Contributed TCAs:

- ▶ Available in the Public Utilities Board Note (PUB Note) in the audited financial statements.
- ▶ If it is not, the municipality should contact their auditor to receive this information.
- ▶ **Applicable to Utility assets that have a current net book value and, were donated to the utility, should have amortization of contributed TCAs to offset the utility deficits.**

PUB Schedule 9 & Adjustments

- ▶ Once the PUB Schedule 9 has been completed, including adjustments, review the Net Operating Surplus (bottom line of Blue highlighted box).
- ▶ If it is the greater than \$10,000 or 5% of annual operating expenses for the utility, then the utility must make application to the Public Utilities Board for approval.
- ▶ If there is no deficit after adjustments then no application needs to be made.

Net Revenue before adjustment	-	-	-
Deduct Deficit recovered in Current Year	-	-	-
Deduct Contributed TCAs Current Year (Note 19)	-	-	-
Deduct Capital Grants Current year (Note 19)	-	-	-
Add Amortization of Capital Grants (Note 19)	-	-	-
Add Amortization of Contributed TCAs (Note 19)	-	-	-
NET OPERATING SURPLUS	-	-	-

Example #1: Deficit Calculation

Actual Operating Deficit No Adjustments

NET REVENUES (DEFICIT)	\$ (31,000)	(16,175)	28,913
TRANSFERS			
Transfers to reserve funds		(2,000)	(2,000)
CHANGE IN UTILITY FUND BALANCE		(18,175)	26,913
FUND SURPLUS, BEGINNING OF YEAR		356,412	329,499
FUND SURPLUS, END OF YEAR		\$ 338,237	\$ 356,412



Example #1: Deficit Calculation

Actual Operating Deficit No Adjustments

15. PUBLIC UTILITIES BOARD

The Public Utilities Board (PUB) regulates the rates charged by all water and sewer utilities, except the City of Winnipeg utility and those utilities operated by the Manitoba Water Services Board. PUB has the authority to order any owner of a utility to adopt uniform and prescribed accounting policies. PUB's prescribed accounting policies on tangible capital assets and government transfers do not meet the recommendations of PSAB.

For information purposes, the Municipality has deferred the capital grants it has received in the past for its utilities and amortized them over the useful life of the related tangible capital asset.

No capital grants have been deferred and amortized in these financial statements.

Example #1: Deficit Calculation

Actual Operating Deficit No Adjustments

Net Revenue before grant adjustment	(31,000)	(16,175)	28,913
Deduct Contributed TCAs Current Year (Note 19)		-	-
Deduct Capital Grants Current year (Note 19)	-	-	-
Add Amortization of Capital Grants (Note 19)	-	-	-
Add Amortization of Contributed TCAs (Note 19)	-	-	-
NET OPERATING SURPLUS	(31,000)	(16,175)	28,913

Deficit Amount to Apply for = \$16,175

Example #2: Deficit Calculation

Actual Operating Deficit With Adjustments

	2019 Budget \$	2019 Actual \$	2018 Actual \$
REVENUE			
PROPERTY TAXES	47,165	47,164	47,305
GOVERNMENT TRANSFERS			
Capital	-	71,082	229,187
OTHER REVENUE			
Connection charges	-	650	650
TOTAL REVENUE	47,165	118,896	277,142
EXPENSES			
SEWER			
Collection system costs	42,165	77,295	55,035
SEWER AMORTIZATION AND INTEREST			
Amortization	16,500	16,590	16,590
TOTAL EXPENSES	58,665	93,885	71,625
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	(11,500)	25,011	205,517
TRANSFERS			
Transfers from (to) utility fund	-	(5,000)	(5,000)
CHANGE IN UTILITY FUND BALANCE	(11,500)	20,011	200,517
FUND SURPLUS, BEGINNING OF YEAR	733,132	733,132	532,615
FUND SURPLUS, END OF YEAR	721,632	753,143	733,132

Example #2: Deficit Calculation

Actual Operating Deficit With Adjustments

16. PUBLIC UTILITY BOARD

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Sewer Services:	Unamortized			Unamortized
Description of Utility	Opening	Additions	Amortization	Ending
	Balance	During Year	During Year	Balance
Vita Wastewater Utility	437,625	71,082	9,602	499,105

Example #2: Deficit Calculation

Actual Operating Deficit With Adjustments

	Budget	2019	2018
Net Revenue before grant adjustment	11,500	25,011	205,517
Deduct Contributed TCAs Current Year (Note 19)		-	-
Deduct Capital Grants Current year (Note 19)	-	71,082	-
Add Amortization of Capital Grants (Note 19)	-	9,602	-
Add Amortization of Contributed TCAs (Note 19)	-	-	-
NET OPERATING SURPLUS	11,500	(36,469)	205,517

Deficit Calculation:

$$\$25,011 - \$71,082 + \$9,602 = (\$36,469)$$

Deficit Amount to Apply for = \$36,469

Example:#3: Deficit Calculation

No Deficit After Adjustments

Total expenses	<u>223,215</u>	<u>276,959</u>	<u>273,352</u>
NET OPERATING SURPLUS	56,216	(12,560)	763
TRANSFERS			
Transfers from (to) operating fund	(17,442)	12,015	-
Transfers from (to) capital	(28,630)	-	-
Transfers from (to) reserve funds	<u>(10,144)</u>	<u>(10,144)</u>	<u>59,664</u>
CHANGE IN UTILITY FUND BALANCE	<u>\$ -</u>	(10,689)	60,427
FUND SURPLUS, BEGINNING OF YEAR		<u>1,180,109</u>	<u>1,119,682</u>
FUND SURPLUS, END OF YEAR		<u>\$ 1,169,420</u>	<u>\$ 1,180,109</u>

Example:#3: Deficit Calculation

No Deficit after Adjustments

19. Public Utilities Board

The Public Utilities Board (PUB) regulates the rates charged by all water and sewer utilities, except the City of Winnipeg utility and those utilities operated by the Manitoba Water Services Board. PUB has the authority to order any owner of a utility to adopt uniform and prescribed accounting policies. PUB's prescribed accounting policies on tangible capital assets and government transfers do not meet the recommendations of PSAB.

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Water services:

Description of Utility	Unamortized Opening Balance	Additions During Year	Amortization During Year	Unamortized Balance Ending
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Oakville Utility	481,853	-	22,180	459,673
	<u>\$ 8,791,424</u>	<u>\$ -</u>	<u>\$ 344,606</u>	<u>\$ 8,446,818</u>

Example:#3: Deficit Calculation

No Deficit after Adjustments

		2019	2018
Net Revenue before grant adjustment	56,216	(12,560)	763
Deduct Contributed TCAs Current Year		-	-
Deduct Capital Grants Current year	-	-	(34,405)
Add Amortization of Capital Grants	-	22,180	22,180
Add Amortization of Contributed TCAs	-	-	-
NET OPERATING SURPLUS	56,216	9,620	57,348

Calculation

$(\$12,560) + \$22,180 = \$9,620 = \text{no deficit}$



Deficit Application

1. Identifying Information
2. Deficit Type and Year
3. Deficit Information
4. Proposed Method of Recovery
5. Utility Information
6. Attachments Required



Deficit Application

What must be submitted:

1. Completed Deficit Application Form
 2. PUB Schedule 9 Form
 3. Council Resolution Approving Deficit and Recovery Method
 4. Explanation of Deficit
- ▶ Failure to submit all pieces required for an application will result in it not being accepted by Board Staff.
 - ▶ Timeliness is important.
 - ▶ Other considerations: If a Utility has revenues stemming from previously approved Deficit Rate Riders or Debenture Surcharges collected on Utility rates, that revenue should be excluded when determining whether or not the Utility has experienced a deficit. PUB has asked that these revenue lines be added to the auditors templates for Schedule 9.



Deficit Application - Identifying Information

WATER AND/OR WASTEWATER UTILITY OPERATING DEFICIT APPLICATION

DEADLINES FOR FILING DEFICITS

Actual Deficit

April 1st in following year

Anticipated Deficit

As soon as known

Budgeted Deficit

April 1st

MUNICIPALLY OWNED UTILITY

PRIVATELY/CO-OP OWNED UTILITY

MUNICIPALITY/OWNER NAME:

UTILITY NAME:

APPLICATION DATE: UTILITY CONTACT:



Deficit Application - Deficit Type & Year

Check the appropriate box to indicate the type of deficit being applied.

ACTUAL DEFICIT

ANTICIPATED DEFICIT
s. 165(2) of *The Municipal Act*

BUDGETED DEFICIT
s. 164(4) of *The Municipal Act*

* For definitions of the type of deficit you may be applying for, please refer to [Board Order No. 151/08](#) and [93/09](#).

Deficit year(s) being applied for:



Deficit Application - Section A

A. DEFICIT INFORMATION

1. Reason(s) for the deficit(s):

2. Amount of Revenue Deficit:

\$	<input type="text"/>
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3. Accumulated Surplus (Deficit) at December 31 of prior year:

\$	<input type="text"/>
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4. Utility Reserve Fund Balance at December 31 of prior year:

\$	<input type="text"/>
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Deficit Application - Section B

B. PROPOSED METHOD OF RECOVERY

1. State proposed method of recovery with rationale:

1(a). Rate Rider over 1, 2, or 3 years in the amount of:

Year 1,

Year 2, and/or

Year 3.

\$	
\$	
\$	
\$	

Note: If proposing more than 3 years for rate rider, please use the "other" method and provide calculations and explanation.

1(b). Draw-down from the accumulated surplus account of the Utility in the amount of:

\$	
----	--

1(c). Withdrawal from utility reserves:

\$	
----	--

1(d). Other method, please explain:

Deficit Application - Section C

C. UTILITY INFORMATION

1. Total number of ratepayers connected to the system.

2. Indicate most current year financials available on Manitoba Municipalities Online (MMO) or provide most current audited financials as attachment.

3. Effective date of last rate revision:

Board Order Number:

4. Statement on current rate adequacy.

5. Please attach current rate structure including:

5(a). Details of current rate structure (flat or metered)

5(b). Minimum quarterly charge

5(c). An indication of rate increases from current rates or minimum quarterly bills.



Deficit Application - Section C

6. Expected date of next rate review:

7. Prior revenue deficits within last 5 years:

Year	Amount	PUB B/O #



Deficit Application - Section D

D. ATTACHMENTS REQUIRED:

1. Council Resolution with respect to deficit and proposed recovery.
2. Completed PUB Schedule 9.
3. Rate Structure (For Municipalities - Schedule A of By-Law)

NOTE: Processing times will vary depending on completeness of the application.

Send completed form via email to: publicutilities@gov.mb.ca



Deficit Recovery Methods

1. Funds Surplus and/or Utility Reserves
2. Rate Riders or Flat Rate



Deficit Recovery Methods

- ▶ A Utility is required to apply to the Board for approval of a deficit, to explain the cause in detail, and to advise how it proposes to recover the deficit, i.e. from fund surplus, the reserve fund, by a temporary rate rider or flat rate (over a specified time period, or a combination of these methods).
- ▶ The Board encourages user-pay rate models, therefore Utility funds should be used for deficit recovery, or collected from Utility customers.
- ▶ For deficits that appear to occur year over year, it is likely the Utility needs to revise its rates. An application for revised rates is required along with the deficit application. This may also be ordered by the Board as a condition of deficit approval.
- ▶ Depending on the method selected by the Utility for recovery, the Board may require a Public Notice to be published.



Deficit Recovery - Funds Surplus

- ▶ Recovery from the Funds Surplus is a transfer from the Surplus of the Utility to recover the deficit.
- ▶ The Utility must first check to see if recovery from the Surplus is an option to apply to the Board.
- ▶ First calculate the working capital for the Utility using the following formula:

	YEAR
Fund Surplus/(Deficit)	
Deduct: Tangible Capital Assets	
Add: Long-Term Debt	
Add: Utility Reserve	
Working Capital Surplus/(Deficit)	
Total Operating Expenses	
20% of Operating Expenses	



Deficit Recovery - Funds Surplus

- ▶ If the Working Capital exceeds the target, 20% of operating expenses, then the deficit can likely be recovered using this method.
- ▶ If the Working Capital meets or is below the target, a combination of the fund surplus and a rate rider deficit recovery method should be considered.
- ▶ If the Working Capital is in deficit, Surplus recovery is not a viable option.
 - ▶ Rate Rider required.



Deficit Recovery - Utility Reserves

- ▶ Check the balance on Schedule 6 of the Municipal Audited Financial Statements.
- ▶ Ensure if there is more than one Reserve fund for the Utility in deficit, that they are all totalled.
- ▶ Calculate the Working Capital for the Utility.
- ▶ Review the Utility's five year Capital or Maintenance plan, to check if reserve funds are appropriated for a specific purpose.
 - ▶ If so then this is not a deficit recovery option.
- ▶ Note: Using the reserve fund to recover a deficit will reduce the Working Capital Surplus, as it is a factor in the calculation.
- ▶ This recovery method can be used as a partial recovery, and is usually combined with another recovery method such as a rate rider, or flat fee.



Deficit Recovery - Rate Rider

- ▶ A rate rider is a temporary increase to Utility rates and is recovered from Utility Customers based on consumption, measured by a meter.
- ▶ This method supports the user-pay principle and is used where Utilities have meters.
- ▶ Best practice is to recover the deficit over the least amount of time as possible, to ensure future generations are not paying for deficits from previous generations (inter-generational in equity).
- ▶ Recovery times are typically 1 to 3 years, however for large multiyear deficits recovery of 5 years have been considered and approved by the Board.
 - ▶ Recoveries in excess of 3 years are rare and at the discretion of the Board.
- ▶ Recovery of rate riders must be tracked and separated from the Utility revenues.
- ▶ Rate Riders must stop when the Board Order directs them to stop.
 - ▶ The deficit is to be recovered through a rate rider of \$XX.XX over a period of X years or until the amount of \$XX,XXX is recovered, whichever comes first.



Deficit Recovery - Flat Rate

- ▶ Similar to a Rate Rider, a flat rate deficit recovery is a temporary increase to Utility rates and is recovered from Utility Customers.
- ▶ This method is used where Utilities do not have meters. All users pay the same amount.
- ▶ Best practice is to recover the deficit over the least amount of time as possible, to ensure future generations are not paying for deficits from previous generations (inter-generational in equity).
- ▶ Recovery times are typically 1 to 3 years, however for large multiyear deficits recovery of 5 years have been considered and approved by the Board.
 - ▶ Recoveries in excess of 3 years are rare and based on evidence before the Board.
- ▶ Recovery of flat rates must be tracked and separated from the Utility revenues.
- ▶ Flat Rates for deficit recovery must stop when the Board Order directs them to stop.



Deficit Recovery - Flat Rate

- ▶ In instances where there is a mix of ratepayers, metered and unmetered, the user-pay principle should prevail, and metered customers should pay based on use.
- ▶ The Utility in this instance could propose unmetered customers pay a flat recovery rate based on a calculation of average use from a similar meter size.
- ▶ For Utilities that do not have meters and have various connection sizes, a flat rate could be calculated based on the residential dwelling (one Residential Equivalency Unit = REU) and multiplied based on the REUs per customer assignment.
- ▶ Any proposed recovery by the Utility must explain in detail why they are requesting this recovery and be supported by calculations.



How to Calculate:

1. Rate Rider
2. Flat Rate



Rate Rider Calculation

- ▶ Rate Rider calculation:

$$\frac{\text{Deficit Amount}^* / \text{Consumption}}{\text{Years to be Recovered}}$$

*If proposing a rate rider to recover multiple years of deficits, the deficit amount is the total of all years being applied for

- ▶ If water consumption is not stable, use an average or the lowest consumption to ensure the deficit can be recovered.
- ▶ Note: Revenues from previous ongoing rate riders for deficit recovery need to be subtracted, this step should have already been completed in the deficit calculation.



Rate Rider Calculation - Example #1

- ▶ Single deficit (1 year of deficit to be recovered)
- ▶ Deficit - \$120,500
- ▶ Water Consumption - 115,000 cubic meters
- ▶ Calculation:

$$\frac{(\$120,500 / 115,000)}{2 \text{ Years}} = \text{Rate Rider } \$0.52 \text{ per cubic meter}$$

Rate Rider Calculation - Example #2

- ▶ Multi-Year deficit with deficit recovery revenue removed:

2013 operating deficit	\$	120,215		
2014 operating deficit	\$	250,042		
2015 operating deficit	\$	200,456		
2016 operating deficit	\$	74,698		
2017 operating deficit	\$	55,469		
2018 operating deficit	\$	45,614		
Total operating deficits incurred	\$	746,494		
Less: Deficit rate rider revenue 2019	\$	95,424		
Outstanding deficit amount	\$	651,070		
Divided by 115,000 cubic meters	\$	5.66		
Divided by 5 years	\$	1.13	per cubic meter	

Rate Rider Calculation - Example #3

- ▶ Deficit Recovery for utilities that use gallons as the unit of measurement
- ▶ Deficit - \$10,589
- ▶ Water Consumption - 2,139.89 thousand gallons
- ▶ Recovery Period - 2 years

$$\frac{(\$10,589 / 2,139.89)}{2 \text{ Years}} = 2.47 \text{ per 1,000 gallons}$$

2 Years



Flat Rate Calculation

- ▶ Flat Rate - all customers treated equally:

$$\frac{\text{Deficit Amount} / \text{Total Number of Customers}}{\text{Years to be Recovered}}$$

- ▶ Flat Rate - based on REU's:

$$\frac{\text{Deficit Amount} / \text{Total Number of REU Assignments}}{\text{Years to be Recovered}}$$

Note: Number of Total REUs is not the same as Total Customers

Flat Rate Calculation - Example

▶ Flat Rate all customers equal:

▶ Deficit - \$36,469

▶ Total Number of Customers - 120

$$\frac{(\$36,469 / 120)}{3 \text{ Years}} = \$101.30 / 4 \text{ quarters} = \$25.33 \text{ per customer per Quarter}$$

▶ Flat Rate based on REU's:

▶ Deficit - \$47,912

▶ Total REUs - 412.5

$$\frac{(\$47,912 / 412.5)}{3 \text{ Years}} = \$38.72 / 4 \text{ quarters} = \$9.68 \text{ per REU per Quarter}$$



Frequently Asked Questions



Frequently Asked Questions

1. What is the meaning of “When calculated for regulatory purposes”?
 - This means the calculations account for any adjustment allowed or approved by the Board when calculating the deficit. For example, the deficit calculation includes the removal of capital grant revenue and addition of grant amortization.
2. What happens if operating deficits are not reported to the Board?
 - If deficits are not reported to the Board, the Utility is not compliant with the Board and in contravention to *The Municipal Act* requirements. The deficit will remain until it is recovered from ratepayers, the longer it is left the larger the intergenerational inequity or recovering from future generations. There is also the possibility to incur more deficits resulting in larger rate riders and increases to ratepayers.



Frequently Asked Questions

3. What if there is a deficit from a previous year, does it still need to be recovered and is an application required?
 - Yes all deficits are required, as per *The Municipal Act*, to be approved by the Board if the deficit is over \$10,000 or 5% of expenses.

4. Can a deficit be recovered from the General Fund? From Taxes?
 - Deficit recovery methods are approved by the Board. The Utility can request one of these recovery methods through the General or Taxes, however it is very unusual that the Board would approve this methodology. There is an issue of subsidization from taxpayers that are not Utility customers from the General or taxes, and the Utility is to be treated as a standalone entity. Debt should not be moved from the Utility to General.



Frequently Asked Questions

5. For deficits that result because of large one-time operating expenditure occurring in a future year, and the Utility is forecast to incur a deficit because of this expenditure. Should this be reported or applied for now?
 - If the Utility has time to submit a rate study to increase rates, possibly increasing the reserve contribution, to save for the large expenditure the Utility should consider this. If a deficit is anticipated, yes the Utility can apply for the approximate deficit amount, however audited numbers and actual deficit is usually the best practice. The Utility should consider the impact on customers if it does not have adequate surplus or reserves to recover the deficit and is applying for a rate rider. If the actual audited deficit amount is higher or lower than the anticipated amount by \$10,000 or 5% of expenses, an adjustment will have to be made once the audited financial statements are available. The Utility will have to apply to the Board to review and vary the rate rider.
6. If the Board approves a Deficit Application, does the Water & Wastewater By-Law need to be revised?
 - This depends if there is a section in the Water and/or Wastewater By-law for deficit recovery or rate riders. Rate Rider duration may not coincide with the approved rate schedule. The Utility will have to read the bylaw carefully.



Frequently Asked Questions

7. Does a working capital deficit have to be reported to the Board. If so, how do we recover this deficit?
 - Utilities do not have to apply for the approval of working capital deficits to the Board. Working capital is one measurement of how the Utility is doing. However, each Utility should calculate the working capital annually to assess its performance. Chances are if there is a working capital deficit, rates should be reviewed and there could also be an operating deficit.

8. The Utility has a “pretty big” working capital surplus. In reviewing the forecast for the utility rates, it appears rates will likely be inadequate next year, can the Utility purposely run a deficit to avoid a rate increase? Do rates have to increase now?
 - The Utility should not purposely run a deficit, however if there is working capital surplus to recover the deficit from the Utility. It can be used as a method of recovery in the application. A rate adequacy study should be started at this time.



Frequently Asked Questions

9. The Utility will not be in deficit if the amortization expense is removed, can the amortization expense be removed from the Net Operating Deficit?
 - The amortization expense cannot be removed from the deficit amount, this is not a Board approved adjustment. Grant Amortization may be adjusted which is a Board approved regulatory adjustment.

10. Should the revenue from deficit rate riders and one-time connection fees be included in the deficit calculation?
 - These revenues for deficit recovery rate riders and one time connection fees, should be tracked on a separate line item in the audited financial statements or have the ability to be calculated separately and sent to the Board with the deficit application. The Utility should request this to be completed by the Municipal Auditor on the Schedule 9 template. These revenues should be removed as they are being collected for a specific purpose. However, in the instance of connection fees, there could be an argument made to include or exclude them depending on the Utility's position.



Frequently Asked Questions

11. Can a deficit be recovered through future surplus?

- The Utility may apply to recover deficits through future surplus for the Board to consider. This is rarely done and the Utility will need to provide a strong argument to do so. If the Utility is already in working capital deficit chances are it will take a couple years to be in a surplus position, and that the Board would not allow this type of recovery. The “kicking the can down the road” analogy is not an advisable strategy.

12. The Municipal Auditor did not complete the PUB Note. The Municipal office keeps our own records of capitalization of amortization grants (using a listing from MWSB). Do we need a confirmation from the auditors that they concur with the deferred capital grant amortization?

- If there is no PUB Note in the audited financial statements, the Utility will have to request the Municipal auditor to include it in future years. The Utility should provide all financial information to the auditor, such as MWSB financial info, to prepare an accurate PUB Note for the audited financials statements.



Frequently Asked Questions

13. The Utility deficit is small, does it still have to be reported?

- The Utility must apply to the Board if the deficit exceeds \$10,000 or 5% of the Utility operating expenses. If the Deficit is under both of these amounts it does not have to be applied for. You can notify the Board via email or letter to advise that there is no deficit to recover and provide the calculation.

14. How detailed does the reason for deficit explanation need to be?

- The reasons should be more specific than increase in expenses or decrease in revenue, and provide what specific expense increased or why revenues decreased. Amortization should no longer be used as a reason for deficits. If rates have been revised since 2010, amortization expense or PSAB is no longer a legitimate reason for a deficit.



Frequently Asked Questions

15. The Municipality does not want to recover the deficit as a rate rider, but as a flat rate instead, can the Utility request this?
- The Utility can request this recovery, it should provide strong evidence to the Board as to why they are requesting this. The Utility should include why this recovery is being proposed if there are meters present. The Utility should also comment on the large users, as to why they would be paying the same as a residential dwelling with less use and smaller meters.



Resources

Resources

- ▶ **Board Order No. 151/08 Water and/or Sewer Utilities Financial Reporting Requirements:** <http://www.pubmanitoba.ca/v1/pdf/08water/151-08.pdf>

- ▶ **Board Order No. 93/09 Regulatory Requirements - Rate Setting, Required due to Adoption of the Public Sector Accounting Board Accounting Standards for Local Government:**

http://www.pubmanitoba.ca/v1/proceedings-decisions/orders/pubs/93_09.pdf

This Order can also be found on the Water and Waste Water Website.

- ▶ ***The Public Utilities Board Water and Wastewater Guidelines***

http://www.pubmanitoba.ca/v1/pdf/water/board_order_guidelines_for_preparing_rate_application.pdf

Resources

- ▶ *The Municipal Act, Section 164(4) & 165(2) Deficit Approval*

<http://web2.gov.mb.ca/laws/statutes/ccsm/m225e.php>

- ▶ **PSAB Reference Manuals:**

Public Sector Accounting Board (PSAB) Generally Accepted Accounting Principles (GAAP) for Manitoba Municipalities: Tangible Capital Assets - Reference Manual (Auditors)

Public Sector Accounting Board (PSAB) Generally Accepted Account Principles (GAAP) for Manitoba Municipalities: Financial Statement Presentation and Disclosure - Reference Manual (Municipalities)

https://www.gov.mb.ca/mr/mfas/mfas_psab.html



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The background features abstract, overlapping geometric shapes in various shades of blue, ranging from light sky blue to deep navy blue. These shapes are primarily located on the left and right sides of the frame, leaving a large white central area.

Thank you